MARKET SEGMENT REPORT **FAMILY STYLE RESTAURANTS** 159

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Restaurant Business

A BILL PUBLICATION

DECEMBER 10, 1989

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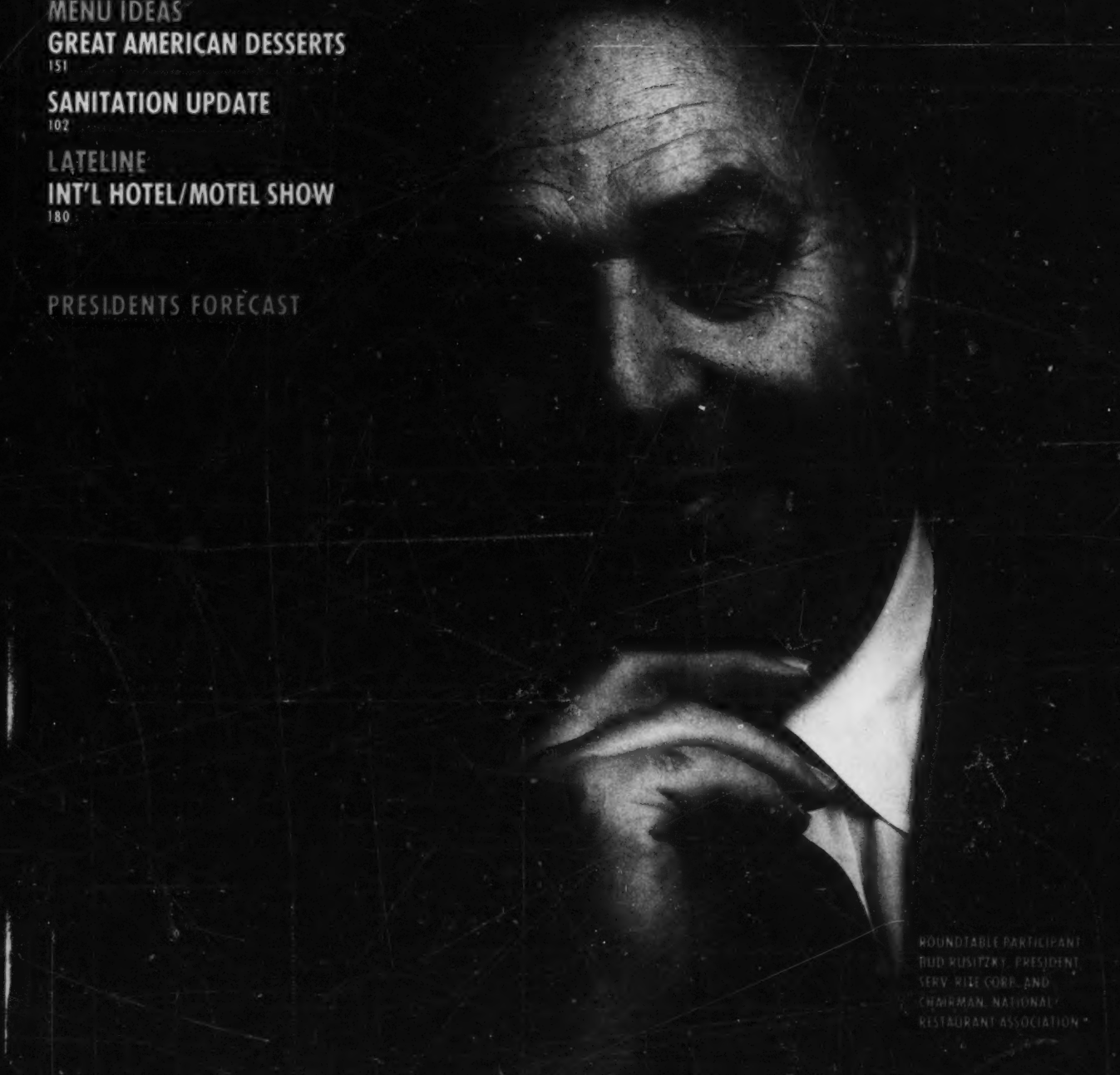
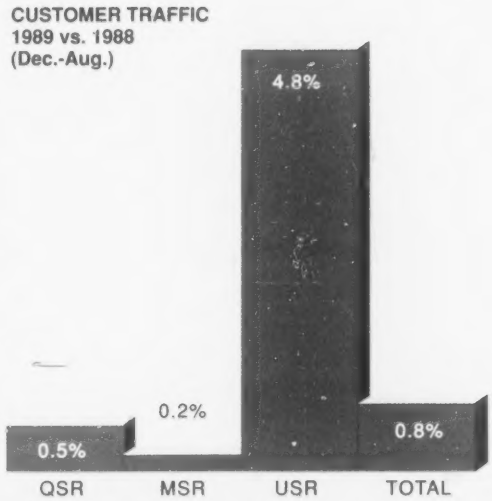


ROUNDTABLE PARTICIPANT BUD RUSITZKY, PRESIDENT, SERV-RITE CORP. AND CHAIRMAN, NATIONAL RESTAURANT ASSOCIATION

THE HARD FACTS SHAPING OUR INDUSTRY

BUSINESS BAROMETER



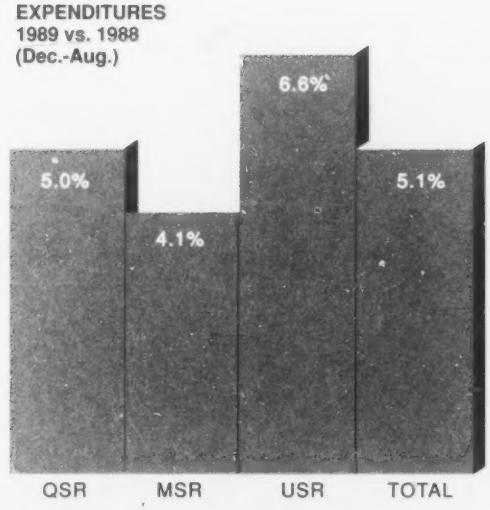
Heavy Traffic

Traffic counts for the nine months ended August 1989 were up a strong 4.8% at upscale restaurants over the same period a year ago, according to GDR/CREST, a service of NPD Research.

Meanwhile, both quick-service and midscale operators had to struggle with nearly flat traffic counts of 0.5% and 0.2%, respectively.

During that same period, the market as a whole was also flat. Total customer traffic for the restaurant industry increased only 0.8%.

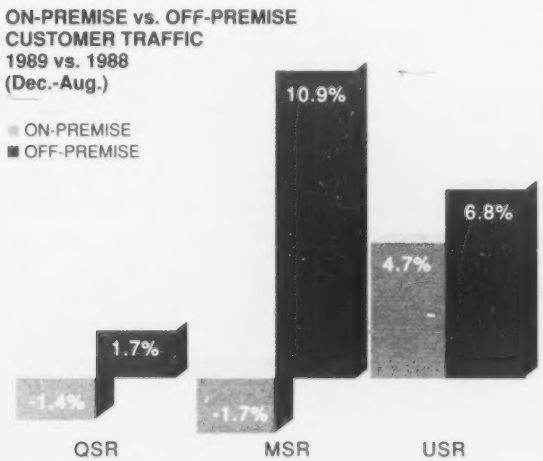
SOURCE: GDR/CREST



Expenditures Climb

With the largest gain in customer traffic, upscale operators enjoyed a moderately strong 6.6% increase in expenditures. Quick-service restaurants, despite sluggish traffic counts, were nonetheless able to achieve increased expenditures of 5.0%, indicating that much of this increase is due to price increases. Similarly, expenditures at midscale restaurants increased 4.1% for the first three quarters of 1989 versus the same period a year ago. Expenditures at all restaurants climbed 5.1%.

SOURCE: GDR/CREST



Take-out Driving Traffic

While overall customer traffic was up 0.8%, take-out has clearly been driving customer counts. In the quick-service segment, less than 40% of all customers eat on-premise: off-premise dining grew by 1.7%, while on-premise dropped by 1.4%. The trend was even more apparent at midscale restaurants, where on-premise dining declined by 1.7% but take-out traffic jumped 10.9% versus a year ago.

Off-premise dining now represents more than 16% of traffic at midscale restaurants. Upscale operators enjoyed both a 4.7% increase in on-premise and a 6.8% rise in take-out.

Off-premise, however, represents only 7% of all traffic at upscale restaurants.

SOURCE: GDR/CREST

RESTAURANT BUSINESS

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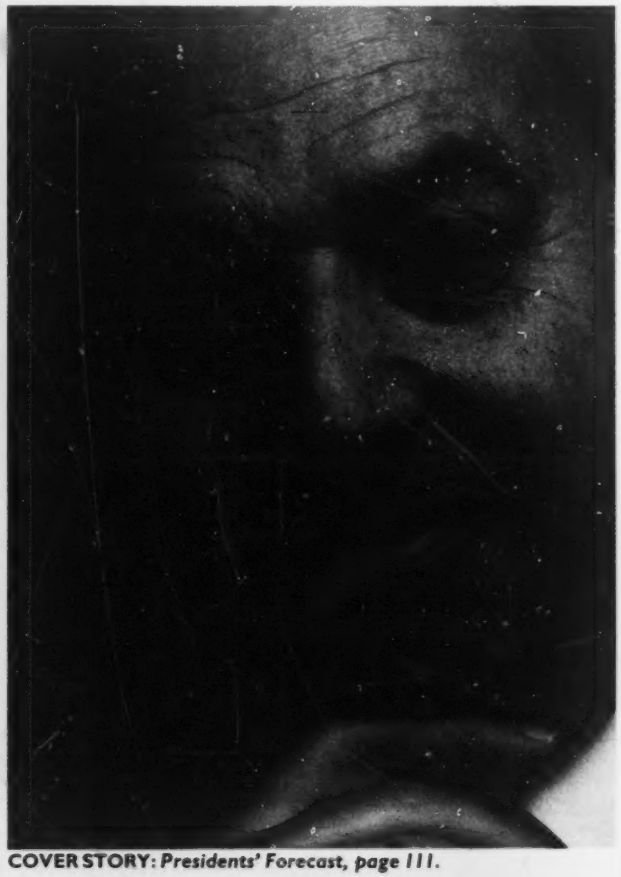

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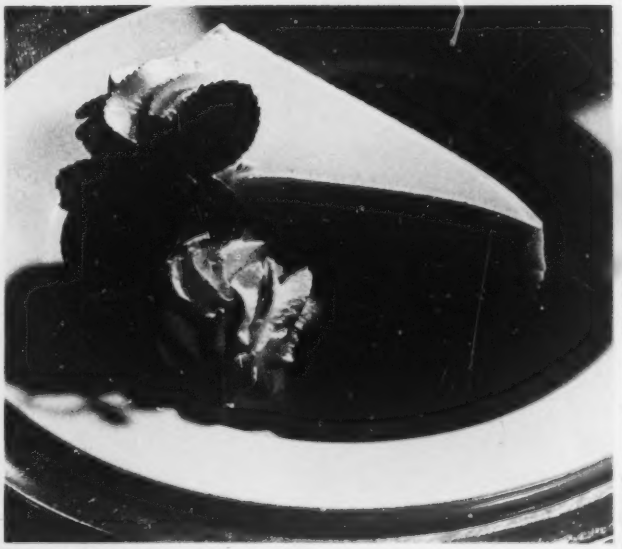

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COVER STORY

PRESIDENTS FORECAST. *Restaurant Business* magazine's Presidents Forecast 1990 was a no-holds-barred think-tank comprised of top industry leaders. The scope of the discussion included such issues as government legislation, market saturation, the economy, shifting consumer demographics, menu development, the labor shortage, and food safety 111

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Cover photo of Bud Rusitzky by Phil Matt

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FEATURES

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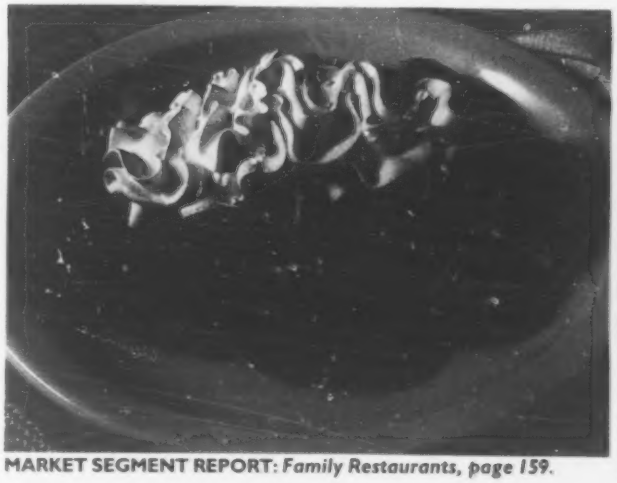
REPRINTS, INDEX AVAILABLE

Restaurant Business now has available reprints of the **1989 RESTAURANT GROWTH INDEX** and the **1989 MAJOR FORCES IN FRANCHISING**. The reprints are $5 per copy. Direct inquiries to: Editor Peter Berlinski, *Restaurant Business*, 633 Third Ave., New York, NY 10017.

Results of the *Restaurant Business*/Deutsch, Shea & Evans exclusive **MANAGEMENT CAREER SURVEY** were published in the *Restaurant Business*. The full text of the 40-page report is now available for $45. Direct inquiries to: David Warhaftig, DS&E, 485 Fifth Ave., New York, NY 10017; (212) 687-8100.

The second annual **CENTER-OF-PLATE** Foodservice Conference for Operators, Distributors, Meat Packers & Processors will be held in Chicago April 2 to 4. For more information, contact Hilarie Hoting, AMI, PO Box 3556, Washington, DC 20007; 703-841-2400.



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CUTTING-EDGE CUISINE

The next decade will bring a continuing surge of restaurants that have gone beyond specializing in authentic dishes; now the emphasis is on using exotic ingredients. This article takes a comprehensive look at the influence of ethnic cuisines on upscale, midscale, and fast-food menus.

MENU IDEAS

PASTA

Because of its marketable appeal, this versatile low food cost item continues to show up on every table, adapting to myriad cross-cultural and ethnic influences.

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HAMBURGER

As the major players continue to play hardball and regional chains vie for market share, the burger remains an American favorite.

SPECIAL FEATURE

TURNAROUND STRATEGIES

Former McDonald's, Burger King, and Pepsico guru Donald Smith has tripled the profits of Perkins family restaurants over the past three years. His recipe for turnaround success involves such human resources programs as improved franchisee relations, and more training of managers and employees. On the Independent side, Walter Conti, who secured his stellar reputation at the Conti Cross Keys Inn in Doylestown, PA, has turned around the Pipersville Inn. He was able to transform it into a successful operation, grossing nearly $1 million this year.

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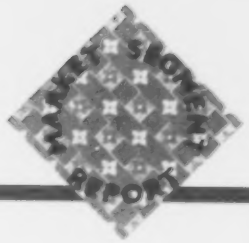
FAMILY STYLE

RESTAURANTS



Although traffic counts are flat, changing customer demographics point toward a brighter future.

By Kevin Farrell

The family restaurant segment has faced many challenges in recent years. Traffic counts have been flat, due in large part to intensified competition from fast-food chains on one side and midprice casual-theme restaurants on the other. Competition within the midprice segment is intense, as well. This has forced increased emphasis on offering customers more variety and good price/value.

Meanwhile, family restaurants have not taken advantage of the additional revenue opportunities from take-out sales. The segment has also been rocked by takeovers and mergers that involved many of the major players, moves that caused a certain amount of turmoil and disruption.

The upside is that the midprice family restaurant segment is well positioned for the future. Its two major customer bases—families and seniors—are segments of the population that are expanding. This should fuel traffic count increases well into the future.

Most chains are taking hard looks at their menus, adding items to broaden appeal and extend into other dayparts; yet, at the same time, they are deleting poor sellers to streamline operations. And remodeling efforts aim at moving the chains into the '90s with bright and contemporary decor.

CHALLENGES. "We've got fast-food chains breathing down our necks," says Clark Jones, founder and chairman of 120-unit JB's Restaurants based in Salt Lake City. "When they offer omelet sandwiches for breakfast, the chains are taking our traditional customers."

The fight for market share is intense. "Our figures show that breakfast

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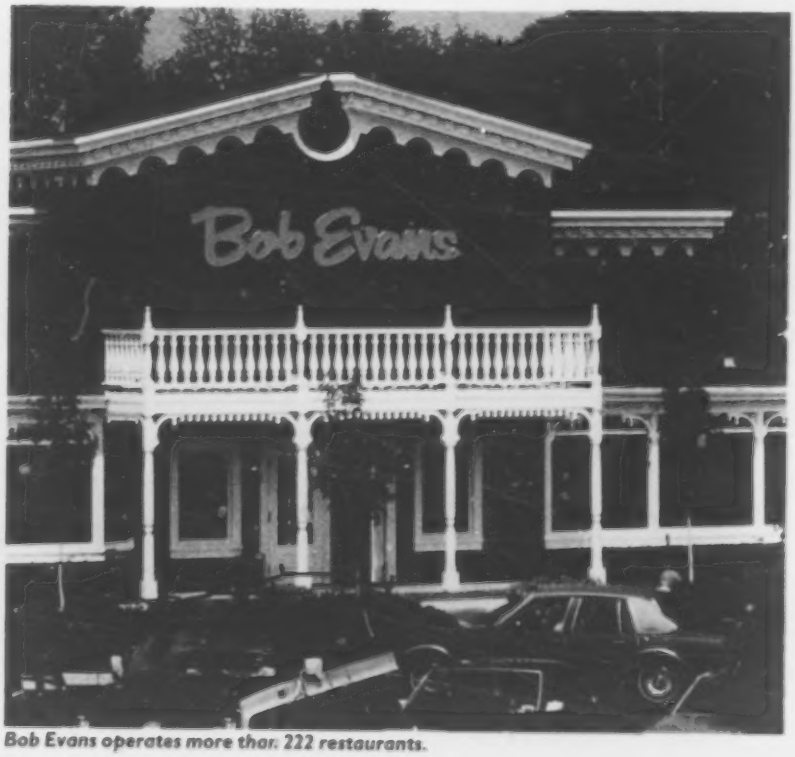

Bob Evans operates more than 222 restaurants.

sales—our major meal period—are declining," says Jon Ostrov, vice president of marketing for Country Kitchen, a division of Minneapolis-based Carlson Companies. "We're searching for a new base, as a market segment and as a chain."

According to CREST, a service of NPD Research, Park Ridge, IL, traffic at midprice family restaurants has been flat for the period August 1988 to August 1989. Prices in this segment have risen about 4% in the last year—roughly corresponding to the U.S. inflation rate.

Most executives agree that price increases have nearly reached the limit, at least for now.

"We're overbuilt, it's that simple," says Bob Wood, executive vice president and chief operating officer of the restaurant division of 222-unit Bob Evans Farms, based in Columbus, OH.

Because the bulk of the customers are families and seniors on limited budgets, price/value is of paramount importance.

PRICE/VALUE. "We have to face the fact that this market is about price/value, more than other factors," says Steve Petisse, vice president of marketing for North Hollywood, CA-based International House of Pancakes (IHOP). "The store design, the menu, and service are all important, but the price/value perception is critical."

"Because we're balanced between the fast feeders on one end and the casual restaurants on the other, our pricing strategy is important," agrees Ostrov. "Of course, it depends on the individual market. We have more flexibility in some markets than in others. But, we really have to hold the line on prices and stay with our competitors. If we get even a little out of line, we can get into trouble."

"Obviously, pricing is a very sensitive subject for our chain," says Jones of JB's. "Whenever we raise prices, we always lose a certain percentage of business, so it is imperative that we hold the line. We were forced into one small increase—in the 3%-to-5% range—this year, and we anticipate another in 1990.

Another disadvantage for midprice family restaurants is that, for the most part, they are unable to take advantage of the additional revenue opportunities from take-out.

International House of Pancakes offers a new line of chicken breast sandwiches with various toppings. The addition was created to capture lunch business.

"It's true that we can't be experts at the take-out business," says Jones. "But, for the customers who come inside our restaurants, we offer speedy service and a friendly face to greet and wait on people."

"With our menu and table service, it is virtually impossible for us to capitalize on the take-out trend," admits Wood of Bob Evans.

"Take-out is not a priority for us," says D.W. Evans, chairman and CEO of Cracker Barrel Old Country Stores Inc. "We have it, but we don't promote it." Cracker Barrel's research indicates that its customers like to sit down and enjoy their meals. "Our research shows that some consumers feel that our competitors are rushing them through the meal," says Evans.

TURMOIL. Compounding existing uncertainties, this market segment has endured a certain amount of merger and acquisition activity in recent years. Segment leader Denny's was purchased by a 54-member team of managers in 1986. Then, it became a takeover target, pursued by many of the big names in the industry. Denny's was eventually sold to TW Services, the owner of Spartan Food Systems, the number-two Hardee's franchisee, and Quincy's Steak Houses. TW Services was subsequently acquired by Coniston Partners.

Friendly Restaurants, a regional chain based in Wilbraham, MA, was bought by Perkins earlier this year. The chain is now being integrated into that system.

CoCo's, originally part of the Grace Restaurant Group, is now owned by Restaurant Enterprises Group Inc. Bakers Square and Village Inn are both now bouncing back after parent VICORP Denver finally managed to absorb some troublesome acqusitions—including a number of old Sambo's locations. IHOP has become employee-owned, while keeping up its string of 80-plus "up" quarters.

All this action has increased competition but has also fueled consumer confusion and management turnover—both serious difficulties in any market segment. But, they are especially so in one as volatile and competitive as the family restaurant segment.

Most analysts and executives are optimistic about the future of the family

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market segment. "We think that the midprice family restaurant is capturing customers who went to quick-service restaurants in the past," observes Dave Jenkins, vice president of marketing for NPD Research. "Many of these chains are successfully appealing to younger families—people who have grown up on fast food."

"In the past, we had been squeezed by fast food and casual restaurants, but I think we are emerging from that competitive disadvantage," claims IHOP's Petisse. "If we listen to our customers' wants and needs, we'll continue to be strong for at least 20 years."

The customer bases that these chains cater to are rapidly increasing. By offering full meals at reasonable prices, family restaurants have traditionally attracted older customers. The 65 and older population is growing quickly. It increased by 25% between 1980 and 1987, and it will continue to grow through the year 2020, according to the National Restaurant Association (NRA).

While the graying of America bodes well for these restaurants over the long term, the short-term future of the family segment clearly lies with young families who have grown used to eating out and are looking for a good and reasonably priced dining experience.

CUSTOMER BASE. Says Petisse of IHOP, "We're seeing a real change in our customers. Some people think all our customers are over 65, but that's far from the truth. There are more young couples with kids. The bulk of our business is in the 25-to-55 age group."

The segment has to compete with fast-food chains for customers.

"Cracker Barrel's customer base is so diverse that it is unfair to characterize it in any one way," says Evans. Cracker Barrel garners over 21% of its consumers from the $55,000-plus income level.

CREST figures indicate that a preference for midscale dining increases with age. While the midscale segment captures approximately 21% of dining-out occasions in the 35- to 44-year-old age group, it provides 42% of the meal occasions for people aged 56 to 74, and 45% for consumers above the age of 75.

Jenkins indicates that these demographic patterns are favorable, but midscale restaurant chains must adapt to changing needs. "There are more younger families who are a sophisticated customer base. They want more exciting cuisine."

The CREST study that pinpointed the increased interest of seniors in midscale dining also asked about menu preferences. They voted for nonfried fish, poultry and potatoes, salads, vegetables, soups, and nonfrozen desserts. Not coincidentally, these are the kinds of menu items being added to midscale family restaurant bills of fare.

TARGETING MENUS. Indeed, the battle for market share is being fought on menus. Some chains have eliminated menu items—even in the face of protests from loyal customers.

"Our menu had gotten too top-heavy and overly complicated," says Wood of Bob Evans' menu. "We had to make some subtractions, as painful as that might be."

Others agree that it is exceptionally

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Breakfast is an important daypart for Cracker Barrel.

hard to remove an item from the menu once it gets on. Menu items develop constituencies very quickly, and removing an item can be more trouble—in a public relations sense—than it is worth.

Denny's, with 1,200 units in 40 states, has reduced its menu by 25% over the last year, according to Sue Henderson, vice president of advertising and promotion for the Irvine, CA-based chain. A new menu was rolled out systemwide last October. "If you looked at this menu, you might think that we have expanded our offerings, but we haven't," says Henderson. "There is more variety achieved using fewer ingredients."

Denny's new menu is 10 pages long, with four sections of color photographs. The main sections are "Day Breaks" breakfast fare; "Soups, Salads, & Sides"; "Sandwich Specialties"; and "Dinner At Denny's. Prices range from 70¢ (for applesauce) to $7.95 (for a steak and shrimp entree).

IHOP has made numerous changes to its standard menu over the last three years. "Our menu has what we call 'treat appeal'," says Petisse. "We're marketing items that are available only at IHOP."

The major menu item added by IHOP in line with this marketing strategy has been its "harvest grain and nut pancakes," with five different grains and three kinds of nuts. After three years of development, the pancakes have now been rolled out to 98% of the chain. Although priced higher than most IHOP items, the pancakes are selling well, Petisse claims. "These cakes sell for $3.35 to $4.00, depending upon the market," says Petisse. "But they have met with virtually no price resistance." The new pancakes are aimed at IHOP's core breakfast customer. But they were also designed to attract new patrons.

Another addition is a line of chicken sandwiches. "We offer a standard chicken breast plus a choice of toppings," says Petisse. Cheese, bacon, avocado, and other toppings are available, for prices ranging from $4.25 to $5.45. The chicken sandwiches were added to boost lunch business, which Petisse claims has been accomplished.

For Bob Evans, the question of menu tinkering is especially touchy, because of customer loyalty. "About 26% of our customers eat at our restaurants once a week," says Woods. "That's an incredible percentage of repeat business. But it has a downside as well. With that kind of loyalty, it is difficult to change anything without alienating a segment of our customer base."

Bob Evans has made menu changes in recent years, and reformulated some standard products. "Clearly, we're not a leader in this area," says Wood. "With our geographic locations and our brand loyalty, we are more likely to follow changes in the marketplace than lead them," he admits.

However, Bob Evans is moving in the direction of a healthier, more nutritious approach. The chain added charbroiled catfish to the menu. It also offers healthy breakfast fare such as egg substitutes and hot oatmeal.

Country Kitchen has upgraded its menu development process and given it top priority. "We needed to change our menu more to keep up with consumer

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This segment's customers are very concerned with price/value.

Country Kitchen has upgraded its menu development process.

FAMILY STYLE RESTAURANTS

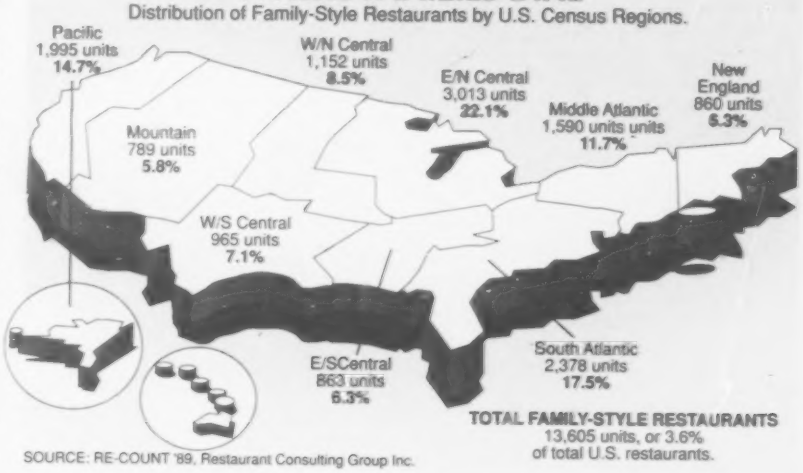
demand," Ostrov says. "We're aiming at changes every six months." Country Kitchen tries to predict what consumers in its markets will be looking for two years from now and "backs up" the menu development process from there.

"For example," says Ostrov, "Let's say that for spring 1991, we have menu 'slots' that we think will be taken by combination dinner platters. We'll formulate some potential products—which we probably already have in the works—and begin to test them." That process includes focus groups, menu product screenings, testing various formulations, getting suppliers to provide differing grades of ingredients for taste and quality tests, in-store testing, comment cards in stores, and checking for operational feasibility.

"This is more sophisticated than we

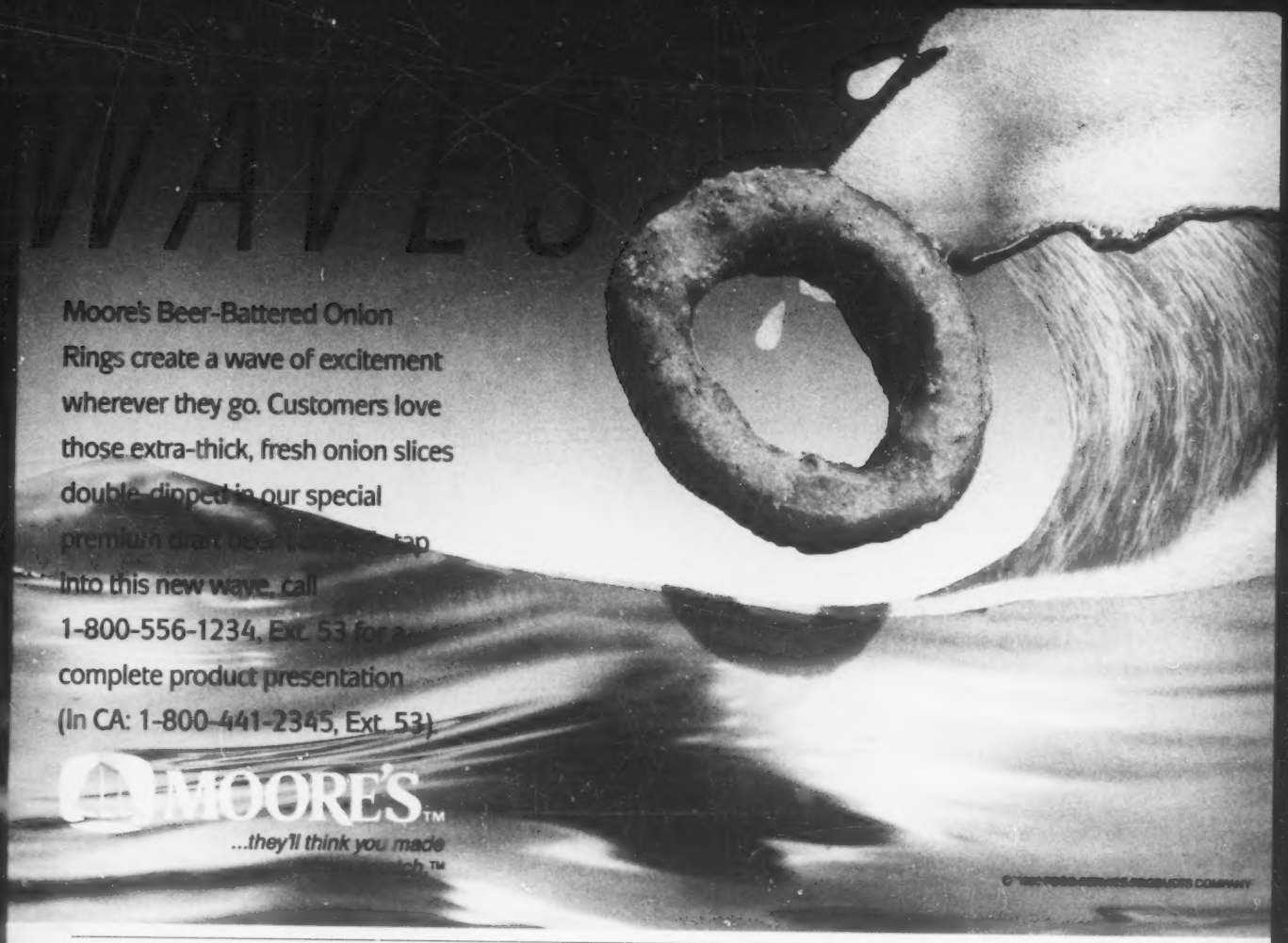
WHERE FAMILIES DINE

Distribution of Family-Style Restaurants by U.S. Census Regions.



TOTAL FAMILY-STYLE RESTAURANTS
13,605 units, or 3.6%
of total U.S. restaurants.

SOURCE: RE-COUNT '89, Restaurant Consulting Group Inc.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TOP FAMILY-STYLE RESTAURANTS

	1988 Sales	Units
Denny's Irvine, CA	$ 1 B	280
Big Boy Warren, MI	$ 1.0 B	350
Shoney's Nashville, TN	$750 M	643
Friendly Wilbraham, MA	$600 M	848
Perkins Memphis, TN	$375 M	341
IHOP North Hollywood, CA	$291 M	448
Bob Evans Farms Columbus, OH	$285 M	221
Waffle House Norcross, GA	$250 M	650
Marie Callender Orange, CA	$245 M	148
Village Inn Denver, CO	$232 M	256

have been in the past," claims Ostrov, "But the market is so much more competitive, that we've had to respond more effectively."

Ostrov is reluctant to provide specific details on menu items in test, but he says that a new menu will be introduced in early 1990. Country Kitchen's new menu is designed to offer more variety but actually has fewer items than past menus.

Some family restaurants have found success by focusing their menus on one item. One such operation is Zehnder's in Frankenmouth, MI.

The family-operated family restaurant is well-known for its chicken-dominated menu. It sells over 11 tons of chicken per week, according to Albert Zehnder, executive vice president.

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Zehnder's "flagship meal" is the family chicken dinner, an all-you-can-eat meal of fried chicken with all the fixings.

This large independent operator serves about 1 million customers a year, garnering $12 million in annual sales. Besides the main restaurant, Zehnder's also operates a 125-seat coffee shop.

Because they are in competition with the casual-theme restaurants that occupy the price niche right above them,

Many chains are changing menus to broaden their customer appeal.

family restaurants have had to upscale their decor as well. Lighter, brighter, more accessible units are what chains like IHOP, Denny's, Country Kitchen, and Cracker Barrel are building today.

Five hundred-unit IHOP is moving away from its small A-frame buildings set on small parking lots and is building upscaled units with 150 seats in many new locations. The chain is also refurbishing existing units in an attempt to expand older sites.

Denny's is remodeling, too, according to Henderson. "Within five to seven years, we will have remodeled 75% of the chain," she says. "And, by then, we'll probably be ready to start over again. The remodeling program is currently on schedule."

Country Kitchen has just unveiled a new unit with a "residential" look, according to Ostrov. It was developed in concert with a committee of subfranchisors, who are particularly powerful in the Country Kitchen organization.

"They are the ones who will pay to build it and who will operate it, so it certainly makes sense that licensees have a say in what it will look like," says Ostrov. "We were trying to capture a more contemporary, but still 'countrified' look with more 'curb appeal'."

Ostrov is unwilling to describe the unit in more detail, pending final approval by the licensees, but he is confident that the chain will begin building the new stores in 1990.

Although the demographics bode well for midprice family chains and independents, many challenges remain. Those operations that offer friendly service, good price/value, and contemporary menus and decor will continue to profit well into the future.

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